

TAX TREATMENT OF NONPROFIT ORGANIZATIONS

by
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A capstone project submitted to Johns Hopkins University in conformity with the
requirements for the degree of Master of Arts in Public Management

Baltimore, Maryland
December, 2014

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Joelle Cannon
Decision Memo
To: Senator Tom Coburn
From: Tax Policy Staff
Re: Tax Treatment of Nonprofit Organizations

Action Forcing Event

Recent statistics reveal nonprofit hospitals, universities and other tax-exempt organizations are bringing in billions of dollars in revenue annually.¹ A 2013 watchdog investigation exposed extensive fraud and abuse throughout the charitable sector.² The Government Accountability Office (GAO) is currently conducting a review of the Internal Revenue Service's (IRS) ability to examine the tax-exempt status of these groups.³ It is widely expected Congress will consider significantly reforming the tax code in the next two years, which could include reexamining the expansive tax-exempt benefits for many entities.

Statement of the Problem

Nearly 1.6 million tax-exempt organizations are recognized by the IRS.⁴ Many of these nonprofit groups exist to address social inequalities or provide an educational or humanitarian benefit to society. A growing number, however, may fall short of providing a truly charitable benefit for society. In fact, some nonprofit groups today more closely resemble for-profit businesses than they do a traditional half-way house, Habitat for Humanity or the Red Cross.

¹ Amy S. Blackwood, Katie L. Roeger, and Sarah L. Pettijohn, "The Nonprofit Sector in Brief: Public Charities, Giving, and Volunteering," *The Urban Institute*, 2012.

² Kris Hundley, and Kendall Taggart, "America's 50 Worst Charities rake in nearly \$1 billion for Corporate Fundraisers," *Tampa Bay Times*, June 6, 2013.

³ Senator Tom Coburn M.D., Letter to Government Accountability Office Director Gene L. Dodaro, July 9, 2013.

⁴ "2013 Data Book," *Internal Revenue Service 55B*, September 30, 2013, 56.

In some cases, such as the National Football League (NFL), these organizations funnel significant portions of donated funds to their own executives and personnel.⁵ Others, like the Kids Wish Network, divert charitable donations to for-profit fundraisers rather than to the needy they claim to help.⁶ If a nonprofit organization serves the interests of only a few or resembles the private sector behaviors, it is appropriate to question their tax-exempt status.

From labor unions to professional sports leagues, multi-million dollar organizations across the country operate similar to for-profit businesses but pay almost nothing in federal taxes. Many, such as prominent academic institutions and credit unions, hold billions of dollars in assets and generate revenue more often associated with that of large companies. Consider, more than 60,000 education-related nonprofits claimed more than \$270 billion in revenue and over \$900 billion in assets, based on 2013 figures.⁷ Likewise, assets of the credit union industry went from \$610 billion in 2003 to over \$1 trillion in 2012.⁸

Other tax-exempt groups operate under the pretext of philanthropy but are really tax shelters for the well-off and provide a benefit to questionable nonprofit directors instead of serving those in need. In 2013, an investigation by the Tampa Bay Times, CNN, and the Center for Investigative Reporting revealed the 50 worst charities in

⁵ Daniel Kaplan, "Roger Goodell's NFL Compensation Exceeds \$44M In 12-Month Period," *Sports Business Daily*, February 14, 2014.

⁶ Kris Hundley, and Kendall Taggart, "America's 50 Worst Charities rake in nearly \$1 billion for Corporate Fundraisers," *Tampa Bay Times*, June 6, 2013.

⁷ "IRS Exempt Organizations Business Master File," *National Center on Charitable Statistics*, December 2013.

⁸ Darryl E. Getter, "Policy Issues Related to Credit Union Lending," *Congressional Research Service*, July 8 2014.

America.⁹ Their inquiry found dozens of these charities divert most donations to private fundraising companies or the bank accounts of nonprofit executives.¹⁰ The money spent by all 50 charities on hired telemarketers, nearly \$1 billion of the \$1.3 billion raised, “would have been enough to build 20,000 Habitat for Humanity homes, buy 7 million wheelchairs or pay for mammograms for nearly 10 million uninsured women.”¹¹

Given the opaque nature of tax data, little is known about the financial operations or lucrative nature of the nonprofit sector. Out of about 1.6 million tax-exempt organizations, 591,000 filed full Forms 990 with the IRS, as of December 2013. These organizations reported a combined \$2.1 trillion in revenue and \$4.7 trillion in assets.¹² Though scant details are available in an easily accessible manner for taxpayers or lawmakers, when combined with industry-specific data, these estimates suggest an extensive amount of revenue generating activity remains untouched by the current income tax code.

The Joint Committee on Taxation concluded that in just one case, that of nonprofit hospitals, their tax-exempt status led to at least \$2.5 billion in lost federal revenue in 2002.¹³ This is roughly \$3.3 billion in today’s dollars. Charitable deductions for donations to health care organizations will result in \$4.9 billion in lost federal revenue

⁹ Kris Hundley, and Kendall Taggart, “America’s 50 Worst Charities rake in nearly \$1 billion for Corporate Fundraisers,” *Tampa Bay Times*, June 6, 2013.

¹⁰ William Higgins, Dave Stanton, and Mike Davis, “The 50 Worst, Ranked By Money Blown On Soliciting Costs,” *The Tampa bay Times*, November 15, 2013.

¹¹ Kris Hundley, and Kendall Taggart, “America’s 50 Worst Charities rake in nearly \$1 billion for Corporate Fundraisers,” *Tampa Bay Times*, June 6, 2013.

¹² “IRS Exempt Organizations Business Master File,” *National Center on Charitable Statistics*, December 2013.

¹³ “Nonprofit Hospitals and the Provision of Community Benefits,” *Congressional Budget Office*, December 2006.

in 2014.¹⁴ Nonprofit hospitals also have access to tax-free bond financing for construction, costing the government another \$3.8 billion in lost revenue in 2014.¹⁵ Combined, these three major tax benefits for nonprofit hospitals cost the federal government at least \$12 billion annually.

Even more, Americans give about \$300 billion of their own money annually to nonprofits,¹⁶ and the charitable tax deduction will decrease federal revenue by an estimated \$46 billion in 2014.¹⁷ Taxpayers also support charities through government grants. Over 1,400 federal programs offer grants to nonprofit organizations, and in 2008, \$38 billion (eight percent) of all federal grant spending was directed to nonprofits.¹⁸

With billions of federal dollars and private donations at stake, this preferential treatment leads to an uneven playing field in the private and nonprofit sectors. Businesses must compete with nontaxed entities—as in the case of the credit union and banking industries. Similarly, within the charitable sector, each dollar donated to a fraudulent or suspect charity is a dollar siphoned from groups providing clothes, food, and shelter to those in need.

Should Congress ignore the growing matter of for-profit organizations avoiding income taxes through their nonprofit status, millions of Americans will continue to pay higher taxes to compensate for this lost revenue and increased federal for these groups. This may also lead to a decrease in charitable activity if truly altruistic organizations no longer can benefit from American's generosity.

¹⁴ "Analytical Perspectives, Budget of the United States Government, Fiscal Year 2015," *Office of Management and Budget*, 207.

¹⁵ *Ibid.*

¹⁶ Katie L. Roeger, Amy S. Blackwood, and Sarah L. Pettijohn, "The Nonprofit Almanac 2012," *The Urban Institute*, 90.

¹⁷ "Estimates of Federal Tax Expenditures For Fiscal Years 2012-2017," *Joint Committee on Taxation*, February 1, 2013, 37-39.

¹⁸ "Nonprofits," *Pew Charitable Trusts: Subsidy Scope*, last modified June 30, 2013.

History

The notion that certain organizations and social activities should not be subject to federal taxation is an idea as old as the income tax itself. While the most familiar of these exclusions is extended to charitable groups, many other entities are also exempt from federal taxes.

Over the last 100 years, Congress has greatly expanded the legal concept of “nonprofit,” adding varying categories of organizations and activities to those considered tax exempt. Most federal law governing the tax-exempt sector is found in Sections 501, 502 and 503 of the Internal Revenue Code. These provisions have grown as Congress responds to special requests for targeted tax exemptions.

Given this longevity, little cohesiveness exists in Congress’ approach to providing this benefit. The overall tenor of congressional action, however, demonstrates generosity in granting tax immunity, not restricting it. Organizations with religious and educational endeavors were exempted from taxes in the Tariff Act of 1894, and have been so in every ensuing income tax bill.¹⁹ More than a century later, with passage of the Patient Protection and Affordable Care Act in 2010, Congress added a new category exempting qualified nonprofit health insurance issuers from federal taxes.²⁰ This haphazard approach to lawmaking created a complex labyrinth of tax exemptions with dozens of categories and extensive regulations for nonprofits.

¹⁹ “Historical Development and Present Law of the Federal Tax Exemption for Charities and Other Tax-Exempt Organizations (JCX-29-05),” *The Joint Committee on Taxation*, April 19, 2005. Presented before the House Committee on Ways and Means.

²⁰ “Report to the House Committee on Ways and Means on Present Law and Suggestions for Reform Submitted to the Tax Reform Working Groups. (JCS-3-13)” *The Joint Committee on Taxation*, May 6, 2013.

With enactment of the first modern income tax in 1913, Congress continued the existing exemptions for charitable, religious, and educational groups (501(c)(3)), while adding several others, including social welfare organizations (501(c)(4)) and business leagues and trade associations (501(c)(6)).²¹ Today, these three categories account for more than 1.2 million of the 1.6 million tax-exempt groups.²² Congress largely left this section of tax law alone in the first half of the 20th century, with the exception of adding a few new tax-exempt categories, such as for entities created by Congress and various employee benefit or retirement funds.²³

Following World War II, however, some nonprofit organizations began working closely with for-profit entities, leading to blurred lines between these two sectors. Not only were some groups using tax-free income, such as donations, to acquire businesses, but some businesses were funneling money to charities claimed to be tax-exempt. In other cases, “unrelated business activities” conducted by nonprofits were used to generate additional for tax-exempt purposes. While perhaps well-intentioned, this activity grew increasingly suspect. These abuses later led some of the first significant changes to the tax-exempt sector, which took place from 1950 to 1954.²⁴

With passage of the Revenue Act of 1950, Congress created the “unrelated business income tax” to address the growth in for-profit activities conducted by nonprofit entities. This tax applies to certain substantial revenue-generating activities conducted by nonprofits that are not directly related to the tax-exempt purpose of the organization.

²¹ Ibid.

²² “IRS Exempt Organizations Business Master File,” *National Center on Charitable Statistics*, December 2013.

²³ “Report to the House Committee on Ways and Means on Present Law and Suggestions for Reform Submitted to the Tax Reform Working Groups. (JCS-3-13)” *The Joint Committee on Taxation*, May 6, 2013.

²⁴ “Scope of Foundation Rules is Broad; They Grant Exemptions but Tax Business Income,” *Commercial Clearing House*, July 3, 1969.

Prior to this change, nonprofits could conduct business and earn revenue, in some cases in direct competition with tax-paying businesses, and yet not pay tax on these profits, often creating an unfair advantage. Yet even with the creation of this tax, Congress included exemptions. The legislation, for example, allowed certain profits to be exempt from the income tax, including interest, dividends and various types of investment income. Although Congress would later make a few more changes to the unrelated business tax, it has remained largely the same for the last four decades.²⁵

Congress completely restructured the tax code and established the Tax Code of 1954, which established the existing section 501(c) and lists nearly each tax-exempt category.²⁶ In a deviation from its tendency to expand tax-exempt privilege, Congress also chose to withdraw the tax exempt status for a number of financial institutions, such as mutual savings banks, but maintained it for credit unions.²⁷ This is noteworthy given the credit union industry still enjoys tax-exempt status today, despite providing traditional banking services to more than 100 million individuals across the country.²⁸

In the 1960s, a series of congressional reports and investigations into private charitable foundations and a subsequent Treasury Department report paved the way for the next round of significant reforms to nonprofit tax law. Highlighting ongoing concerns with the nature of the activities engaged in by tax-exempt entities, the Treasury Department recommended changes to “six major problems,” ranging from “delay in benefit to charity” to “family use of foundations to control corporate and other

²⁵ Paul Arnsberger, Melissa Ludlum, Margaret Riley, and Mark Stanton, “A History of the Tax-Exempt Sector: An SOI Perspective,” *Internal Revenue Service Statistics of Income Division*, Winter 2008.

²⁶ “Report to the House Committee on Ways and Means on Present Law and Suggestions for Reform Submitted to the Tax Reform Working Groups. (JCS-3-13)” *The Joint Committee on Taxation*, May 6, 2013.

²⁷ “Credit Unions Retain Exemption: Other Savings Groups Lose Out” *Commercial Clearing House*, July 25, 1969

²⁸ Marine Cole, “Why 100 million people bank at credit unions,” *The Fiscal Times*, August 22 2014.

property.”²⁹ The resulting legislation, the Tax Reform Act of 1969, delineated between private foundations and public charities and established a structure of excise taxes to be used as penalty for nonprofit organizations in violation of certain earnings and income standards set in law.³⁰

This same law also significantly affected the nonprofit healthcare sector, by removing any requirement that these institutions provide services for free or below cost. The law provided that instead, nonprofit hospitals must only a “community benefit.”³¹ Today, more than 60 percent of hospitals nationwide are nonprofit 501(c)(3) entities, but bring in millions of dollars in annual revenue. While health and medical care have long been considered charitable, the true business nature of most nonprofit hospitals has changed drastically since the early 20th century. Many of these institutions traditionally accepted patients unable to pay for the medical care. The creation of Medicare and Medicaid, however, changed this, as much of these services previously offered at no charge were now reimbursed by the government.

Much of the tax law governing the nonprofit sector has remained largely unchanged in the last forty years. Additional exemptions, however, continue to be granted, including to veterans’ organizations providing insurance and other benefits, to certain groups providing legal services benefits, and multi-employer plan trusts, among others.³²

²⁹ “Historical Development and Present Law of the Federal Tax Exemption for Charities and Other Tax-Exempt Organizations (JCX-29-05),” The Joint Committee on Taxation, April 19, 2005. Presented before the House Committee on Ways and Means.

³⁰ Ibid.

³¹ Ibid.

³² “Historical Development and Present Law of the Federal Tax Exemption for Charities and Other Tax-Exempt Organizations (JCX-29-05),” The Joint Committee on Taxation, April 19, 2005. Presented before the House Committee on Ways and Means.

Despite the growth and change of the nature of many nonprofit organizations, Congress has made few changes to the laws governing these groups. The IRS recognizes the significant changes and expansion of the tax-exempt sector, acknowledging “Today, the legislation enacted between 1917 and 1969 remain the cornerstone of tax exemption in the United States. However, the tax-exempt sector has grown substantially over the past 2 decades... The activities of tax-exempt organizations have also broadened and new types of tax-exempt organizations have emerged.”³³

More recent changes have introduced a small measure of transparency to the nonprofit sector. In 2007, Congress required the IRS to make the Form 990-T filed by tax-exempt groups available to the public.³⁴ Still, these documents are not easily accessed or understood. While certain online databases exist, such as the GuideStar database of searchable Forms 990, the IRS does not offer a database of aggregate nonprofit financial information or the nature of any punitive federal or state-based actions taken against questionable groups.

In December 2010, the President's National Commission on Fiscal Responsibility and Reform released a comprehensive deficit reduction plan that included a complete overhaul of the tax code, including curtailing deduction for charitable donations.³⁵ Since that time, several members of Congress have proposed various tax reform plans. Perhaps

³³ Paul Arnsberger, Melissa Ludlum, Margaret Riley, and Mark Stanton, “A History of the Tax-Exempt Sector: An SOI Perspective,” *Internal Revenue Service Statistics of Income Division*, Winter 2008, 122.

³⁴ Paul Arnsberger, Melissa Ludlum, Margaret Riley, and Mark Stanton, “A History of the Tax-Exempt Sector: An SOI Perspective,” *Internal Revenue Service Statistics of Income Division*, Winter 2008.

³⁵ “The Moment of Truth,” *The National Commission on Fiscal Responsibility and Reform*, December 2010.

most notably, in February 2014, outgoing House Ways and Means Chairman, Dave Camp issued a widely discussed draft for comprehensive tax reform.³⁶

Chairman Camp's proposal included a number of substantial changes to existing tax-exempt law, but the proposal does not call for an increase in transparency related to these groups. The plan calls for repealing the tax-exempt status of the National Football League and all other professional sports leagues and subjecting tax-exempt organizations to "a 25 percent excise tax on compensation in excess of \$1 million paid to any of its five highest paid employees." The Joint Committee on Taxation estimated this one change, subjecting tax-exempt salaries to an excise tax, could raise \$4 billion in revenue over ten years.³⁷

Further, the Camp proposal acknowledges continued growth in business and for-profit activity by the non-profit sector and seeks to address some of these matters. The discussion draft explains the nature of these activities — "public charities are engaging in more commercial activities than ever before and are using more complex organizational structures to do so. Many organizations, such as AARP, are now earning significant profits licensing their own names to for-profit businesses (which is not taxable to an exempt organization) to avoid engaging in an active trade or business themselves."³⁸

Background

Growth in Size and Scope Nonprofit Organizations

The last forty years has witnessed an explosion in the size and scope of nonprofit entities operating in the United States that are not subject to federal income taxes. In

³⁶ "Tax Reform Act of 2014: Discussion Draft: Section-by-Section Summary," *House Committee on Ways and Means*.

³⁷ Ibid.

³⁸ Ibid.

1976, there were more than 756,500 tax-exempt entities.³⁹ Today, there are nearly 1.6 million.⁴⁰

Many tax-exempt organizations, such as churches, are not required to report financial data to the government.⁴¹ Approximately 591,000 groups currently file a Form 990 with the IRS, providing the details of their financial activities, including revenue, expenses, annual spending on activities related to their nonprofit purpose, and total assets.⁴² This is up from 247,086 nonprofit groups that filed with the IRS in 1975.⁴³ Tax-exempt entities reported \$252 billion in total revenues and \$543 billion in assets in 1975 (in 2001 dollars).⁴⁴ By contrast, filing nonprofit entities reported a combined \$2.1 trillion in revenue and \$4.7 trillion in assets as of December 2013.⁴⁵ Despite their classification as “nonprofit,” the financial standing of these groups more closely resembles that of million-dollar companies.

The Joint Committee on Taxation concludes charities have “have experienced a disproportionate share” of the growth.⁴⁶ In the charitable category alone, there are more

³⁹ “Historical Development and Present Law of the Federal Tax Exemption for Charities and Other Tax-Exempt Organizations,” *The Joint Committee on Taxation*, April 19, 2005, 20. Presented before the House Committee on Ways and Means.

⁴⁰ “2013 Data Book,” *Internal Revenue Service 55B*, September 30, 2013.

⁴¹ “Historical Development and Present Law of the Federal Tax Exemption for Charities and Other Tax-Exempt Organizations (JCX-29-05),” *The Joint Committee on Taxation*, April 19, 2005. Presented before the House Committee on Ways and Means.

⁴² “IRS Exempt Organizations Business Master File,” *National Center on Charitable Statistics*, December 2013.

⁴³ “Historical Development and Present Law of the Federal Tax Exemption for Charities and Other Tax-Exempt Organizations,” *The Joint Committee on Taxation*, April 19, 2005, 18. Presented before the House Committee on Ways and Means.

⁴⁴ “Historical Development and Present Law of the Federal Tax Exemption for Charities and Other Tax-Exempt Organizations,” *The Joint Committee on Taxation*, April 19, 2005, 24. Presented before the House Committee on Ways and Means.

⁴⁵ “IRS Exempt Organizations Business Master File,” *National Center on Charitable Statistics*, December 2013.

⁴⁶ “Historical Development and Present Law of the Federal Tax Exemption for Charities and Other Tax-Exempt Organizations,” *The Joint Committee on Taxation*, April 19, 2005, 22. Presented before the House Committee on Ways and Means.

than one million Section 501(c)(3) organizations⁴⁷ – up from 259,523 in 1976.⁴⁸ This number continues to grow, with the IRS approving nearly 38,000 applications for 501(c)(3) status in FY 2013 alone.⁴⁹ By contrast, in 1976, there were 259,523 charities, with assets valued at \$360 billion and revenue of \$155 billion (both in 2001 dollars).⁵⁰

Some Nonprofit Organizations Similar to For Profit Businesses in Revenue & Assets

Much of the revenue and assets accumulated by nonprofits exists in the education and medical sectors of the 501(c)(3) groups. “In 2001, hospitals held 29 percent of total assets and collected 42 percent of total revenues in the charitable sector. Colleges and universities held 21 percent of the total assets and collected 11 percent of total revenue.”⁵¹ In 2004, of the top ten public charities, by size of total assets, six were major universities, including the top three - Harvard, Stanford, and Yale Universities, and three were medical entities - Howard Hughes Medical Institute, Kaiser Foundation Hospitals, and Shiner’s Hospital for Children.⁵²

Consider the higher education system. 501(c)(3) educational institutions account for 15 percent of the charitable sector and hold billions of dollars in assets. About 78,000 education-related nonprofits filed Forms 990, on which they reported \$285 billion in revenue and \$965 billion in assets.⁵³ Harvard University’s endowment exceeded \$32 billion in 2013, while the endowments of Yale, Princeton, Stanford, and the University of

⁴⁷ “Historical Development and Present Law of the Federal Tax Exemption for Charities and Other Tax-Exempt Organizations,” *The Joint Committee on Taxation*, April 19, 2005, 2. Presented before the House Committee on Ways and Means.

⁴⁸ “2013 Data Book,” *Internal Revenue Service 55B*, September 30, 2013, 56.

⁴⁹ “2013 Data Book,” *Internal Revenue Service 55B*, September 30, 2013, 55.

⁵⁰ “Historical Development and Present Law of the Federal Tax Exemption for Charities and Other Tax-Exempt Organizations,” *The Joint Committee on Taxation*, April 19, 2005, 2. Presented before the House Committee on Ways and Means.

⁵¹ *Ibid.*

⁵² Paul Arnsberger, Melissa Ludlum, Margaret Riley, and Mark Stanton, “A History of the Tax-Exempt Sector: An SOI Perspective,” *Internal Revenue Service Statistics of Income Division*, Winter 2008, 113.

⁵³ “IRS Exempt Organizations Business Master File,” *National Center on Charitable Statistics*, December 2013.

Texas are in the \$18-\$20 billion range.⁵⁴ The exclusion from tax for these investments is very lucrative. “Big endowments such as Harvard’s probably often reap at least \$1 billion annually from capital gains. They pay no income taxes on those gains; individuals pay 23.8 percent. They also pay no income taxes on dividend and interest income,” according to economist Richard Vedder.⁵⁵

A number of professional sports leagues are also tax-exempt nonprofits, including the National Football League, the PGA Tour and the National Hockey League. The NFL is classified as a 501(c)(6) nonprofit organization despite holding over \$1 billion in assets. The NFL’s nonprofit entity received \$184 million from its 32 member teams in 2010.⁵⁶ When combined with subsidiaries, the NFL makes approximately \$9 billion annually.⁵⁷ Meanwhile, the PGA brought in more than a billion dollars.⁵⁸

Credit unions are also tax-exempt, even though providing traditional banking services to millions of Americans. As noted, from 2003 to 2012, the assets of the credit union industry jumped from \$610 billion to more than \$1 trillion.⁵⁹ With extensive growth in membership, revenue and assets, the credit union industry is clearly a for-profit industry, but they remain tax exempt, costing the Treasury at least \$2.1 billion in FY

⁵⁴ “U.S. and Canadian Institutions Listed by Fiscal Year 2013 Endowment Market Value and Change* in Endowment Market Value from FY 2012 to FY 2013,” *National Association of College and University Business Officers and Commonfund Institute*, February 2014.

⁵⁵ Richard K. Vedder, “Cut Off Harvard to Save America,” *Bloomberg View*, February 20, 2014.

⁵⁶ “Form 990: Return of Organization Exempt From Income Tax,” *National Football League*, 2010.

⁵⁷ Dan Daly, “Another Way to Look at the NFL’s \$9 Billion in Revenue,” *The Washington Times*, February 24, 2011.

⁵⁸ “Form 990: Return of Organization Exemption From Income Tax,” *Professional Golfers Association*, 2012.

⁵⁹ Darryl E. Getter, “Policy Issues Related to Credit Union Lending,” *Congressional Research Service*, July 8 2014.

2014.⁶⁰ Even more, credit unions are “the only depository institutions exempt from federal income taxes,” according to the Congressional Research Service.⁶¹

Some Nonprofit Organizations Salaries and Structure Questionable for Tax-Exempt

Status

The structure of some nonprofits may increasingly resemble for profit businesses and not that of charities and tax-exempt member organizations that exist to serve a needy population or provide a service to their members. This is perhaps no clearer indicator of this than the salaries and compensation offered by some nonprofits. It may be concerning that the tax-exempt status of some entities allows for extremely high levels of compensation.

Consider the case of some nonprofit hospitals, which continue to benefit from tax exempt status, yet many medical executives have salaries far exceeding what is often considered appropriate for charitable entities. The average compensation for the chief executive officer position at nonprofit hospitals is more than \$595,000, yet many earn much more.⁶² The chief executive officer of the largest nonprofit hospital in the country, the University of Pittsburgh Medical Center Presbyterian, receives compensation of nearly \$6 million. Other prestigious hospitals, like Barnes-Jewish Hospital in St. Louis and the New York-Presbyterian/Will Cornell Medical Center, pay their top executives

⁶⁰ “Estimates of Federal Tax Expenditures for Fiscal Years 2013-2018 (JCX-97-14),” *The Joint Committee on Taxation*, August 5, 2014. Prepared for the House Committee on Ways and Means and the Senate Committee on Finance.

⁶¹ “Tax Expenditures: Compendium of Background Material on Individual Provisions,” *Congressional Research Service*, December 2012. Prepared for the Committee on the Budget: United States Senate.

⁶² Karen E. Joynt MD, MPH, et al., “Compensation of Chief Executive Officers at Nonprofit US Hospitals,” *JAMA Internal Medicine*, January 2014.

\$2.3 million and \$4.5 million respectively.⁶³ These salaries are dwarfed, however, by the nonprofit NFL, which pays Commissioner Roger Goddell more than \$44 million a year.⁶⁴

Some Nonprofits May Not Serve the Charitable or Tax-Exempt Purpose

It is not just the profits and salaries that may call into question the tax-exempt status of some entities. In many cases, these groups may not necessarily provide much charitable benefit, despite saving millions of dollars on their tax bills. With the revenue and assets mirroring that of the private sector, policymakers would hope this increased revenue would mean an increase in charity for those in need. Yet this is not always the case, which suggests much of the increased revenue flow may be directed to less than charitable activities.

50 Worst Charities in America

Recent investigations reveal countless examples of questionable charitable organizations engaging in unscrupulous activities, such as spending too much money on for-profit fundraisers, using the charity as a shell organization to funnel money for one's personal benefit, and providing very little charity they claim to serve.

A 2013 investigative project launched by the Tampa Bay Times, CNN, and the Center for Investigative Reporting exposed the 50 worst charities in America.⁶⁵ Their work raised serious concerns with the activities and financial structures of dozens of charitable 501(c)(3) organizations, many of which diverted most of their charitable donations to private fundraising companies instead of to charitable activities.

⁶³ Steven Brill, "Bitter Pill: How outrageous pricing and egregious profits are destroying our health care," *TIME Magazine*, March 4, 2013.

⁶⁴ Daniel Kaplan, "Roger Goodell's NFL Compensation Exceeds \$44M In 12-Month Period," *Sports Business Daily*, February 14, 2014.

⁶⁵ Kris Hundley, and Kendall Taggart, "America's 50 Worst Charities rake in nearly \$1 billion for Corporate Fundraisers," *Tampa Bay Times*, June 6, 2013.

Using causes like “Find the Children,” and “Cancer Fund of America,” the 50 worst charities in America raised \$1.3 billion in donations over the last ten years.⁶⁶ Yet, almost none of this money went to find lost children, to support those with cancer, or to any other charitable cause. A \$1 billion the funds raised were used to pay for-profit fundraisers.⁶⁷ A Florida charity, The Kids Wish Network, was declared America’s worst charity. This fake Make-A-Wish Foundation purports to make dreams come true for dying children. Yet, the group gave its corporate fundraisers \$110 million of the \$128 million it raised in the last decade.

Unlike Make-a-Wish, which spends only a small fraction of donations on fundraising, the KWN directs 97 percent of their yearly contributions to fundraisers. In fact, in 2012, KWN raised \$18.6 million and spent only \$240,000 on wishes. In the last 10 years, Kids Wish Network directed \$4.8 million to its founder and his for-profit businesses.⁶⁸ The Florida Attorney General and the Florida Department of Agriculture are investigating the KWN, yet the group has not had its tax-exempt status revoked to date.⁶⁹

Federal Cost and Revenue Losses from Tax-Exemptions for Nonprofit Organizations

Entities exempt from paying federal income taxes receive a substantial financial benefit from the government in return for their nonprofit endeavors. Government funding extended to the nonprofit sector is not only derived from the tax code through their exemption, but also comes from other more direct spending streams. Receiving tax-

⁶⁶ William Higgins, Dave Stanton, and Mike Davis, “The 50 Worst, Ranked By Money Blown On Soliciting Costs,” *The Tampa bay Times*, November 15, 2013.

⁶⁷ Kris Hundley, and Kendall Taggart, “America’s 50 Worst Charities rake in nearly \$1 billion for Corporate Fundraisers,” *Tampa Bay Times*, June 6, 2013.

⁶⁸ Kris Hundley, and Kendall Taggart, “America’s 50 Worst Charities rake in nearly \$1 billion for Corporate Fundraisers,” *Tampa Bay Times*, June 6, 2013.

⁶⁹ Dave Elias, “NBC2 Exclusive: Kids Wish Network being investigated,” *NBC-2*, July 3, 2013.

exempt status also qualifies these groups to receive federal support through grants, subsidized loans, and other financial benefits.⁷⁰

According to the Congressional Research Service, direct federal spending for nonprofit organizations, including grants and payments, totaled \$350 million in 2005, representing the second largest revenue source for charitable organizations.⁷¹ A project by Pew Charitable Trusts determined more than 1,400 federal programs provide grants to nonprofit organizations, and in \$38 billion, or eight percent, of all federal grant spending was directed to nonprofit groups in 2008.⁷²

Not only is the government losing billions of dollars to some organizations that may not be truly deserving of this generosity, but private citizens who choose to donate to these nonprofit groups are also at risk of financial harm. Americans give nearly \$300 billion of their own money every year to nonprofit organizations, which they are allowed to deduct as a charitable donation in many cases.⁷³ The charitable deduction results in billions of dollars of decreased revenue each year and will decrease federal revenue by about \$46 billion in 2014.⁷⁴ Yet, the truly exemplary groups in need of donations may suffer revenue losses when donations are directed to fraudulent groups or those with little charitable purposes.

With limited federal resources it is crucial taxpayer's generosity is provided to accomplish truly worthy endeavors. While many nonprofit organizations across the country meet this standard, the nearly unrestrained growth in size and scope of many

⁷⁰ Molly F. Sherlock and Jane G. Gravelle, "An Overview of the Nonprofit and Charitable Sector," *Congressional Research Service*, November 17, 2009.

⁷¹ *Ibid.*

⁷² "Nonprofits," *Pew Charitable Trusts: Subsidy Scope*, last modified June 30, 2013.

⁷³ Katie L. Roeger, Amy S. Blackwood, and Sarah L. Pettijohn, "The Nonprofit Almanac 2012," *The Urban Institute*, 90. Includes giving to all nonprofits, not solely 501(c)(3) organizations.

⁷⁴ "Estimates of Federal Tax Expenditures For Fiscal Years 2012-2017," *Joint Committee on Taxation*, February 1, 2013, 37-39.

entities not required to pay taxes leaves some question as to their true need of these government benefits.

Key Actors in the Tax-Exempt Discussion

The tax-writing committees in Congress will be the primary leaders in any debate over the tax-exempt sector, should Washington consider reforming the tax code in the 114th Congress. At least two key players in Congress have already introduced tax reform proposals, providing a glimpse into what may be on the horizon for the tax-exempt sector should reform come.

Earlier this year, outgoing House Ways and Means Committee Chairman Dave Camp released the first draft comprehensive tax reform plan including extensive changes to both the individual and corporate income taxes. Although he is retiring, Congressman Camp's proposals will likely resurface in any proposals issued by the new Ways and Means chairman.

Following the November election, if the Republicans remain in control of the House, it is largely assumed Congressman Paul Ryan of Wisconsin will take over at the committee helm. Better known for his sweeping health care reform proposals, Ryan's approach to tax reform is largely undiscovered. Certainly this is the case with his position on tax treatment of the nonprofit sector, with perhaps one noteworthy consideration. Ryan has long been public about his Catholic faith, which could be a factor in this debate, given the influence of the Catholic Charities in the nonprofit sector.

With the Senate very much in play during the 2014 election, it is not yet clear which party will have the majority next Congress. Regardless of who holds the gavel, should Congress take up tax reform in the next Congress, all eyes will be focused on the

Senate Finance Committee. Senator Ron Wyden, a Democrat from Oregon currently chairs the committee, and Senator Orrin Hatch, a Republican from Utah serves as the ranking member. Although Senator Wyden, along with Republican Senator Dan Coats, also previously introduced a comprehensive tax reform plan, it did not include any significant changes to the tax-exempt sector, does not require any increased disclosure, and does not curtail the charitable deduction.⁷⁵

Another prominent voice in Congress during any nonprofit tax debate will be Senator Chuck Grassley, a Republican from Iowa. Grassley and his staff are known for serious oversight efforts aimed at the tax-exempt sector, and he is likely to weigh in heavily on this debate. During the Senate's consideration of the Affordable Health Care Act, Grassley had a provision inserted requiring additional disclosure and transparency for nonprofit hospitals, including the submission of a report to Congress "regarding the levels of charity care, bad debt expenses, unreimbursed costs of means-tested government programs, and unreimbursed costs of non-means tested government programs incurred by private tax-exempt, taxable, and governmental hospitals..."⁷⁶

On the other end of Pennsylvania Avenue, White House officials at the Treasury Department will likely be heavily involved in any rewrite to the tax code and the rules governing the tax-exempt sector. The president's FY 2015 budget made relatively few changes to the tax-exempt sector, but proposed capping the charitable deduction at 28 percent for upper income taxpayers. The budget, however, proposed requiring all tax-exempt organizations that file a Form 990, to do so electronically. It would also mandate

⁷⁵ Senators Ron Wyden and Dan Coats, "The Bipartisan Tax fairness and Simplification act of 2011 (S. 727)," *United States Senate*, April 5, 2011 (112th Congress 2011-2013).

⁷⁶ "Technical Explanation of the Revenue Provisions of the 'Reconciliation Act of 2010,' as Amended, in Combination with the 'Patient Protection and Affordable Care Act' (JCX-18-10)," *The Joint Committee on Taxation*, March 21, 2010, 83.

the IRS make these returns publically available.⁷⁷ Treasury Secretary Jack Lew and his team are certain to play a part in these negotiations, though it is likely their focus will be more on the overall tax number and perhaps not as much with the minutia of changes made to Section 501.

Involvement from constituencies outside the Beltway will also play an integral role in the debate of any changes made to the tax-exempt requirements. This will include religious and charitable groups, tax reform and fiscal hawk groups, and government reform and transparency advocacy organizations.

Active religious organizations, such as the Family Research Council, the Evangelical Free Church of America, the Catholic Charities, and others representing churches and nonprofit across the country will be vigilantly involved in any nonprofit debate in Congress, and certainly so during tax reform discussions. While not a religious organization, the Independent Sector is a particularly active nonprofit advocacy entity likely to make their presence known on Capitol Hill during any consideration of legislation that may affect nonprofit groups.

Additionally, organizations focused on reducing the deficit, reforming the tax code, or cutting spending may also engage in the overall tax reform debate, which will affect the nonprofit sector. Many of these groups, such as the Committee for a Responsible Federal Budget and the Bipartisan Policy Center, have proposed comprehensive tax reform plans that included curtailing charitable tax deduction. Transparency groups, such as the PublicResource.org, OMB Watch, and the Sunlight Foundation, are also likely engage in any discussion surrounding reforms and changes to

⁷⁷ “General Explanations of the Administration’s Fiscal Year 2015 Revenue Proposals,” *Department of the Treasury*, March 2014.

filing and transparency requirements for those groups claiming tax-exempt status. PublicResource.org, is already active on the issue and has sued the IRS, asking the agency to make charities' financial data available in a format that is readable and searchable on a computer.⁷⁸

Policy Proposal

The justification - or lack thereof - for each category of nonprofit organization differs, as Congress granted these exemptions in ad hoc manner. A simpler and standardized approach to federal tax benefits for these groups is needed. Few details about their financial activities and holdings are available however, making sweeping reforms difficult to enact at this time.

Policy Authorization

This proposal is intended to significantly increase the transparency and coordination of private, state, and federal data concerning the nonprofit sector. Access to this information, for both taxpayers and lawmakers, will pave the way for future legislation to completely overhaul the tax treatment of these organizations.

Specifically, this legislation would require the IRS, within one year of enactment, to:

- publish an online, searchable federal database, all IRS audits of tax-exempt organizations (“audit database”);
- establish an online, searchable federal database to track all state-level actions against fraudulent and questionable charities (“state actions database”); and
- establish an online searchable database containing for each tax-exempt entity, certain financial statistics and information, such as total assets, annual revenue,

⁷⁸ Suzanne Perry, “Lawsuit Would Force IRS to Release Nonprofit Tax Forms Digitally,” *The Chronical of Philanthropy*, June 16, 2014.

amounts spent on fundraising, and unrelated business income taxes paid, among others (“nonprofit financials website”).

A provision would be included to ensure the IRS is given full authority to publish all information required for the nonprofit financials website. This will include the authority to waive 26 U.S. Code § 1603, which governs the privacy and disclosure of tax returns.

Despite a lack of across-the-board transparency, some financial details are available for some nonprofit industries, including nonprofit hospitals, educational institutions, and credit unions, as outlined in this memorandum. Further analysis may shed light on the consequences of a decision by Congress to consider these organizations for-profit for purposes of paying federal income tax.

As such, the legislation would direct the Government Accountability Office, in conjunction with the Joint Committee on Taxation, to conduct a comprehensive examination of the social, economic, and financial ramifications of revoking or curtailing the tax-exempt status of nonprofit hospitals, educational institutions, and credit unions. The study would be completed and submitted to Congress within one year of enactment.

While no funds would be explicitly authorized in the bill for the joint GAO-JCT study, the bill would authorize “such sums as necessary,” for the IRS to carry out the mandate to create three new websites and searchable databases.

Policy Implementation

The IRS will be responsible for carrying out the creation of the three new transparency websites, but will retain flexibility in doing so. While publishing the IRS audits can and should be implemented by IRS personnel, the agency should consider if it is more cost effective to contract the services required to establish the other two

databases. Regardless of if the websites are created internally or the work is contracted to a private vendor, the creation of all three databases will require the issuance of regulations and guidelines.

The nonprofit financials website will require detailed coordination with both internal IRS lawyers and those staff with access to the financial information required for inclusion on the database. The IRS should not issue regulations requiring additional paperwork or submissions from filing nonprofit organizations, as the agency already retains access to the details required to complete the database.

In light of constant technological advancements, when enacting legislation authorizing executive branch use of technology, it is inappropriate for Congress to mandate the use of a particular type of technology or specific software programs. As such, in directing the creation of new websites and searchable databases online, sufficient discretion will be left to the executive branch to determine the most timely and efficient technology needed for this endeavor.

Although the legislation would authorize funding to create the three new websites, these funds will need to be provided through the annual congressional appropriations process. It is incumbent upon the IRS to request sufficient funds needed to create the new transparency websites.

The GAO-JCT study of the nonprofit status of hospitals, universities, and credit unions is to be carried out by these two congressional service organizations in adherence to their existing procedures and protocols for all congressionally mandated requests. This often includes consulting with congressional authors of the mandate to ensure full compliance, as well as coordination and information requests from both relevant

executive branch agencies and private entities. In this case, these likely include the Departments of Treasury, Education, and Health and Human Services, and the IRS, as well as private sector representatives for the health, education and credit union industries.

The completed study, findings and recommendations will be publicly available for all members of Congress and taxpayers. In keeping with current practice, no additional funding should be needed to carry out this provision.

Policy Analysis

Rather than entertain a far-reaching overhaul of tax law, this proposal embarks on a transparency expedition, designed to shed light on the nonprofit sector. There are both benefits and limitations to adopting a transparency-based approach to address any public concern, including that of multimillion dollar nonprofit organizations. Generally, requiring increased transparency may be considered a first and achievable step toward meaningful reform, but often lacks the gravitas associated with more tangible policy changes. Similarly, while technology promises much accountability, the government lags behind the private sector in hi-tech advances, calling into question implementation and enforcement feasibility. It is also important to recognize transparency as a stick is limited, especially when not linked directly to an enforcement mechanism.

The most concrete policy goal achieved by this proposal is an increase in the level of information regarding the financial nature and activities on nonprofit organizations made available in a centralized, searchable, and online location, to both the public and policymakers. Conversely, the proposal's greatest shortcoming is the lack of any immediate revocation of any group or industry's tax-exempt status and does not result in

comprehensive reform of Section 501 of the tax code. These and other considerations are outlined in detail for further examination of the proposal.

Transparency is Not a Long Term Solution, but May Eventually Lead to Significant Reforms

Disclosure is generally considered a form of discipline, or a policy “stick,” in that it requires new actions to be taken by a certain party. In this proposal, that action is required primarily of the executive branch, as the IRS is directed to publish certain details of nonprofit organizations, as well as the results of internal IRS audits of and any state regulatory actions taken against these groups. Transparency also can take on the nature of a sermon. The information gained from disclosure may later be used in media or public service campaigns to bring about certain changes.

The disclosure and transparency requirements in this proposal will not immediately eliminate the tax-exempt status of any organization entity considered to be nonprofit. The proposal does not require the IRS to take any punitive actions against known fraudulent entities. With the absence of these measures, the proposal will not result in quantifiable revenue increases to the Federal Treasury. With these limitations, the proposal falls short of immediately reversing the extensive concerns outlined in this memo. This is the most significant failing of the proposal, and it deserves serious consideration from any lawmaker hoping to draft comprehensive legislation curtailing existing nonprofit groups.

Because of the delayed and essentially untraceable results of the impact of transparency and accountability, this proposal lacks some discernible metrics through which policy makers could view success. For example, it would not be possible to track

each taxpayer who used the audits database and chose not to donate to a particular entity they previously planned to support. While this phenomena would occur, these types of successes would be difficult, if not impossible, to quantify in any aggregate form.

Lawmakers wishing to tout specific examples of increased IRS scrutiny, revoked tax-exempt status of questionable groups, or enhanced taxpayer benefits, may find this proposal lacking in the short run. Their patience would likely be rewarded, however, as these case studies and examples would emerge over time.

What it lacks in rapid recourse, however, increased transparency may offset with a different style of discipline – accountability. Exposing on a more widely available scale, the true financial nature of many tax-exempt entities, as well as IRS’s auditing and state regulatory actions, will likely lead to progress in at least four areas.

1. Lawmakers will be more equipped to make informed decisions regarding how specifically the tax code should be changed to reflect the changing nature of nonprofits.
2. The new state actions database would enable each state to prohibit groups with questionable fundraising or those disallowed from other states, from setting up shop within their own borders.
3. Because of access to the IRS audit database and the states actions database, taxpayers will be able to make more informed decisions regarding where donating their money or time.
4. Some entities may voluntarily give up their nonprofit status in light of new disclosure requirements and more centralized public access.

Given the current dearth of information available regarding the true financial nature and behavior of many tax-exempt organizations, it may be unwise for lawmakers

to enact sweeping nonprofit tax reform. Access to the information that would be disclosed in the new nonprofits financials website would provide policymakers with details of the size and scope of many nonprofits. Similarly, the required GAO-JCT study would provide analysis the economic and social impacts of revoking the tax-exempt status of the education, hospital, and credit union industries. Lawmakers could use the insight from these sources to guide the crafting of legislation to address the tax future of many nonprofit groups.

Such advanced preparation is not routine in Congress, which often approves rushed legislation before few have read it or understand any possible ramifications. Information gathering and data analysis before a national headline rushes congressional action, could lead to more thoughtful legislation addressing only those tax-exempt entities truly in violation of the spirit through which nonprofit tax benefits are granted.

The creation of a centralized database of nonprofit financial information and the two additional databases will also enable lawmakers to enact more targeted legislation addressing specific industries or entities no longer deserving of tax-exempt status. This may be particularly beneficial with the charitable organizations, as many investigations reveal numerous are essentially swindling donors and lining their own pockets with the proceeds. Making these details readily available to federal and state officials, as well as to taxpayers, will also allow them to hold these groups accountable.

In some cases, public pressure or outrage based on widely available information from the new requirements could lead to the elimination of special tax treatment for certain organizations. Comptroller General David Walker, echoed this sentiment in

testimony to the House Ways and Means Committee regarding the IRS' ability to monitor the tax-exempt sector and the need for transparency as part of the agency's oversight efforts. His testimony asserted, "Transparency sheds light on entities' practices, which enhances ethical and effective operations and facilitates oversight by the public and others."⁷⁹ Walker further explained the pressure public accountability provides, "Transparency over the operations of the exempt entity provides an incentive to help ensure the governance practices function as intended and when they do not, transparency helps increase the chances that inappropriate behavior will be detected and corrected."⁸⁰

Walker's testimony also advocated increased coordination between the states and the IRS, regarding those groups against which state regulators had taken action. "States and IRS believe that more data sharing would make their oversight more efficient and effective," he acknowledged.⁸¹ While his testimony suggested internal information sharing was needed, this proposal carries that one step further by requiring an online catalogue of state actions, available for both the public and IRS personnel.

A similar phenomenon occurred with the requirement that appropriations earmarks be provided to lawmakers in an electronic and searchable format. Little was known about the nature of congressional earmarks, many of which were directed to lawmakers' favorite local project, to projects owned by friends and family, or projects benefitting campaign donors. As some members of Congress demanded transparency and

⁷⁹ David M. Walker, "Governance, Transparency, and Oversight Are Critical for Maintaining Public Trust," (Statement before the House Committee on Ways and Means,) *Government Accountability Office*, April 20, 2005, 4.

⁸⁰ David M. Walker, "Governance, Transparency, and Oversight Are Critical for Maintaining Public Trust," (Statement before the House Committee on Ways and Means,) *Government Accountability Office*, April 20, 2005, 29.

⁸¹ David M. Walker, "Governance, Transparency, and Oversight Are Critical for Maintaining Public Trust," (Statement before the House Committee on Ways and Means), *Government Accountability Office*, April 20, 2005, 4.

access to information regarding the names, locations, and recipients of earmarks, members of the media and other lawmakers were able to expose many of these earmarks as wasteful or part of a pay-to-play scheme.

These findings, such as Alaska's infamous "bridge to nowhere," called into question the validity of all earmarks and sparked public outrage. Combined with other national earmark scandals, this exposed because of increased public scrutiny, paved the way for the elimination of congressional earmarks. The bridge to nowhere vote, which received only 15 votes in support of eliminating it, occurred in 2005.⁸² Six years later, House Republicans instituted a complete earmark ban.⁸³ Though a microcosm, a series of similar events could occur given more public examination over those organizations that operate tax free in the United States.

On a larger scale, consider the case of Canada, whose revenue agency publishes all audits of nonprofit organizations as well as the Canadian version of the IRS' Form 990. The agency provides the filings of tax-exempt organizations online, in a free, searchable and downloadable format.⁸⁴ In just one example, Canadian officials called attention to questionable fundraising by a charity called Pediatric Aids. After being shut down in Canada, the charity's director relocated to the United States, continuing to divert most donated dollars to inappropriately high levels of fundraising costs.⁸⁵

While the heightened public scrutiny derived from new transparency requirements will likely lead to corrective actions taken by lawmakers, the increased sunshine may also

⁸² "H.R. 3058: U.S. Senate Roll Call Votes 109th Congress – 1st Session: Question: On the Amendment (Coburn Amdt. No 2165, As Modified)," *United States Senate*, October 20, 2005.

⁸³ Erin Kelly, "Some want earmarks back to help Congress pass bills," *USA Today*, October 29, 2013.

⁸⁴ Beth Simone Noveck, and Daniel L. Goroff, "Information for Impact: Liberating Nonprofit Sector Data," *The Aspen Institute*, January 31, 2013, 31.

⁸⁵ "America's Worst Charities - #34: Optimal Medical Foundation," *The Tampa Bay Times*, last updated July 17, 2014.

lead some nonprofits to willingly give up their tax-free status. Major League Baseball, for example, filed as a tax-exempt entity until 2007, when it relinquished this tax preference voluntarily. It has largely been reported the organization did so in light of public disclosure requirements, primarily those of senior executive salaries.⁸⁶ Should transparency requirements lead to a natural weeding out of suspect groups or those wishing not to comply with increased disclosure, there may be a slight increase in federal revenue from this transition. While this is certainly probable, it is another measure of success that remains nearly impossible to track.

GAO acknowledges, “These transparency efforts have enabled civic engagement, and have allowed the public—from ordinary citizens to sophisticated data users—to access information on spending, recipients, and uses of funds. The data’s availability has also provided opportunities for increased oversight to prevent and detect fraud, waste, and abuse of federal funds, and to improve the efficiency and effectiveness of federal spending.”⁸⁷

Transparency is Efficient -- Minimal Startup Costs & Significant Potential Benefit

One of most appealing aspects of the transparency approach of this proposal is the minimal price tag, coupled with the possibility for significant financial benefits in the future. The cost of establishing three new online databases should be weighed against the potential savings for both the Federal Treasury and generous benefactors, as well as the social benefit of redirecting donations to worthy charities.

As government continues to modernize, the cost of providing online transparent information to taxpayers has varied. Fluctuations in cost can depend on the complexity

⁸⁶ Jordan Weissmann, “The NFL is Not a Nonprofit,” *Slate*, September 18, 2014.

⁸⁷ “Federal Data Transparency: Opportunities Remain to Incorporate Lessons learned as Availability of Spending Data Increases (GAO-13-758),” *Government Accountability Agency*, September 2013, 1.

and availability of the required data, as well as the agency's infrastructure for building the online database or the cost of hiring a contractor to do so.

The audits database requires the IRS to post existing internal documents online in a searchable format. The cost of creating this site may include the time to create the online platform, as well as some internal hours spent on "cleaning up" the documents for public consumption and ease of use. The Congressional Budget Office estimated a bill requiring all federal agencies to post more detailed programmatic spending data online would cost \$25 million annually.⁸⁸ Simply requiring an agency to publish existing data and forms online will likely cost significantly less.

The other two proposed websites, the state actions database and the nonprofit financial information, will require more effort, generating a larger cost than the audits database. Combined, these two provisions may more closely mirror the cost associated with the establishment of an existing database of government spending, USAspending.gov. Congress enacted the Federal Funding Accountability and Transparency Act in 2006, which required the creation of an online, searchable database detailing the recipients of nearly \$900 billion in federal spending. Launched in December 2007, USAspending.gov, was designed to provide easily navigable and accessible information for taxpayers and members of Congress.⁸⁹

Initial cost estimates suggested creating and maintaining the new website would cost \$15 million in the first five years. This was, however, based on the assumption that agencies already collected and maintained easy access to the required information, which

⁸⁸ "Congressional Budget Office Cost Estimate: H.R. 3262: Government Results and Transparency Act," *Congressional Budget Office*, February 22, 2012. Ordered by the House Committee on Oversight and Government Affairs on November 3, 2011.

⁸⁹ Garrett L. Hatch, "The Federal Funding Accountability and Transparency Act: Implementation and Proposed Amendments," *Congressional Research Service*. February 3, 2009.

eventually proved untrue.⁹⁰ Although the cost has exceeded this estimate, more recent estimates suggest the cost of transitioning the website to the Treasury Department will be roughly \$4.5 million, while the regular operations and maintenance will be \$1.13 million.⁹¹

Unlike with the data needed to establish USAspending.gov, which was collected from all agencies across the executive branch, the nonprofit financials database requires information already collected by and located only at the Treasury Department. This could significantly reduce the costs associated with implementing this plan, compared to that of USAspending.gov.

The most challenging and likely costly provision in the proposal is that of the state audits database. This will undoubtedly prove labor intensive, as the information is currently scattered among 50 state governments and nonprofit regulatory entities. As such, this portion of the proposal will require more work from IRS officials, in the gathering of information from each state based nonprofits regulator. Assuming these higher costs, when combined with the lower cost of the nonprofit financials website, the cost estimate of these two databases could be similar to that of USAspending.gov.

Taking into account the establishment each proposed websites, it fair to assume implementing the proposal could cost the government at least \$25 million in the first year with start-up and implementation costs, with annual costs of \$10 million thereafter.

Lawmakers often presume the costs of making government spending and other federal actions transparent are offset by a future financial benefit. To substantiate this assumption, however, the financial gain should stem from changes that take place

⁹⁰ Ibid.

⁹¹ “Bureau of the Fiscal Service: FY 2015: Capital Investment Plan,” *Department of the Treasury*.

because of the newly provided information. Yet, as previously noted, difficulty in quantifying any potential gains or successes derived from such disclosure is one of the primary challenges with using increased transparency to spur eventual behavioral changes. In this case, however, a plausible scenario can be constructed which provide insight into significant possible savings from implementation of the proposed databases.

The establishment of the state actions database will result in a centralized location for all nonprofits across the country against which a state regulator has taken some form of disciplinary action. As noted by the *Tampa Bay Times*, there is a significant concern that charities barred from fundraising in one state simply relocate across the border, swindling donors in another state. The establishment of a national database of these actions provides not only the donating public, but also IRS oversight officials, with a centralized location to easily access the names of those charities that should be further reviewed for inappropriate fundraising and failing to meet the standards of federal tax-exempt status.

With the creation of a state audits database, IRS personnel would now be able to apply greater scrutiny to a targeted list of entities already found to be delinquent in at least one state. If they refused, lawmakers could even use this information to instruct the IRS in legislation to immediately revoke the tax-exempt status of certain groups. If only 50 organizations, out of the nearly one million charities across the country, were to lose their federal tax-exempt status from this increased examination, taxpayers would no longer be subsidizing for-profit activities with a generous tax-exempt preference. Even these meager successes could reduce the government's revenue losses by significantly.

Similar to the case of Major League Baseball, the potential for existing nonprofit entities to voluntarily give up their tax-exempt status could generate increased federal revenues. This action is already being considered by the National Football League, which has come under scrutiny for its tax-free status despite clear for-profit endeavors.⁹² Should other professional sports leagues with over \$10 million gross annual receipts follow suit, the Joint Committee on Taxation estimates federal revenue would increase by \$5 million in fiscal year 2014 and by \$109 million over the next ten years.⁹³

No funds are authorized in the bill for GAO and JCT to carry out the review of the education, health care, and credit union industries. As such, this provision will not result in any additional cost to the federal government. Yet, there is potential for increased federal revenue in the future, should their findings lead Congress to curtail or reject all together the tax-exempt status of one or more of these industries. Even if leaving in place the existing benefit for hospitals and institutions of higher education, should Congress, on the heels of the GAO-JCT study, choose to revoke the tax-exempt status of credit unions, this could result in \$2.1 billion in increased federal revenue in a single year. This would rise to nearly \$12 billion over five years.⁹⁴

A substantial social benefit, beyond that of the estimated financial savings, that would be derived from implementing these transparency measures. Many of the examples of fraud and misdirected financial donations proliferated by numerous charities revealed by the Center for Investigative Reporting and the Tampa Bay Times, would be captured

⁹² Adam Stites, "NFL considering dropping tax-exempt status, according to report," *SB Nation*, September 29, 2014.

⁹³ Chief of Staff of the Committee on Taxation Thomas A. Barthold, Letter to Senator Tom Coburn M.D. concerning the PRO Sports Act, May 15, 2013.

⁹⁴ "Estimates of Federal Tax Expenditures For Fiscal Years 2014-2018 (JCX-97-14)," *The Joint Committee on Taxation*, August 5, 2014. Prepared for the House committee on Ways and means and the Senate Committee on Finance.

in the state actions database. Further, any IRS audits of these and other dishonest organizations would also be made public. Raising awareness and publicly exposing fraudulent organizations will enable those who give of their personal means, to better direct their generosity to those groups truly providing charity to those in need.

In just their one study, the Center for Investigative Reporting⁹⁵ found that \$1 billion of the \$1.3 billion raised by only 50 charities, was funneled not to those in need, but to the pockets of for-profit fundraisers.⁹⁵ Assuming even only half of this \$1 billion in misdirected donations, was prevented because of public disclosure, \$500 million in charity would be better used. If that \$500 million were instead given by donors to serious charities, a true benefit to society worth a half-a-billion dollars would occur. Conversely, if taxpayers simply refrained from donating that \$500 million because of their knowledge of a questionable group, then federal savings would be derived from the absence of a charitable deduction claimed on that amount. Even these estimates are severely understated, as they are based on the misdirected use of donations raised by only 50 out of the nearly one million charitable organizations.

Transparency Provisions are Feasible, but will Face Challenges

Because the government is only beginning to catch up to what many consider to be routine technological functions, a discussion of feasibility is appropriate when considering this policy proposal. Implementation and ongoing challenges facing existing government websites, including USAspending.gov and Healthcare.gov, call in to question the executive branch's ability to create a new website or aggregate data for taxpayer use. Despite challenges, these and other government websites are fully

⁹⁵ Kris Hundley, and Kendall Taggart, "America's 50 Worst Charities rake in nearly \$1 billion for Corporate Fundraisers," *Tampa Bay Times*, June 6, 2013.

functioning and meeting at least part of their intended purpose. Through this perspective, policymakers can view the IRS' ability to implement the online database platforms required by this proposal.

Similar to the cost comparisons, reviewing the executive branch's implementation of USAspending.gov offers a glimpse into the possible technological challenges with providing searchable and accurate information online. Implementing USAspending.gov was tremendous administrative and technological undertaking by the executive branch, spearheaded by the Office of Management and Budget.

The programmatic and spending information required to create and maintain USAspending.gov was to be collected from 38 different agencies and existed in varying levels of detail and differing formats, resulting in delayed implementation and gaps in data. A 2010 GAO review of the program's implementation found at least nine federal agencies had failed to submit grant awards to OMB for the database, and OMB was not in compliance with several aspects of the law governing USAspending.gov.⁹⁶ Similarly, this June - six years after the website was supposed to be fully operational - GAO's most recent study found \$619 billion in government awards that were improperly reported and included in USAspending.gov.⁹⁷

While implementation of USAspending.gov has continued to struggle under OMB's jurisdiction, recent activity suggests the IRS may be more prepared to handle these types of transparency and technological endeavors. Recent proposals, including President Obama's FY 2014 budget request, have called for the relocation of

⁹⁶ "Electronic Government: Implementation of the Federal Funding Accountability and Transparency Act of 2006 (GAO-10-365)," *Government Accountability Office*, March 2010, 2-4.

⁹⁷ "Data Transparency: Oversight Needed to Address Underreporting and Inconsistencies in Federal Award Website (GAO-14-476)," *Government Accountability Office*, June 2014, 11.

USAspending.gov, from OMB to the Treasury Department.⁹⁸ Further, a leaked OMB memo opposing legislation to move administration of USAspending.gov from OMB to Treasury, led the Data Coalition’s Hudson Hollister to conclude, “The Treasury Department is eager to take on these challenges,” and the agency has sanctioned one staffer as “executive director for data transparency efforts at Treasury.”⁹⁹

Due to one primary difference between the nonprofits transparency proposal and comprehensive disclosure of government spending, it is reasonable to assume the IRS will not face implementation challenges to the extent of those encountered by OMB with USAspending.gov. GAO’s review of USAspending.gov found OMB’s guidance to the agencies regarding their data submissions for the searchable website was insufficient and unclear, essentially making the submissions voluntary.¹⁰⁰ This proposal, by contrast, requires the IRS to make public almost entirely information currently within its own purview. The IRS will not need to rely upon or aggregate information from other existing federal agencies in order to meet the requirements of this proposal. This should greatly reduce the administrative burden of aggregating information from different sources, while result in far fewer data gaps or errors. The only exception to this is that of the state actions database, which will require IRS to compile information from state nonprofit regulators. This will likely leave this specific database open to challenges more similar to those encountered with USAspending.gov.

In its 2013 assessment of the IRS’ Information Technology (IT) capabilities, the IRS Inspector General for Tax Administration explains “The IRS relies extensively on

⁹⁸ “Fiscal Year 2014: Budget of the U.S. Government,” *Office of Management and Budget*, 143.

⁹⁹ “Leak Reveals White House OMB Effort to Remove Key Provisions from Data Act,” *Data Transparency Coalition*, January 27, 2013.

¹⁰⁰ “Electronic Government: Implementation of the Federal Funding Accountability and Transparency Act of 2006 (GAO-10-365),” *Government Accountability Office*, March 2010, 2-4.

computerized systems to support its financial and mission-related operations.”¹⁰¹ The agency’s IT budget was \$2.3 billion in fiscal year 2013, and more than 7,300 employees work solely on IT matters. Fourteen of these employees work in the office of the chief technology officer.¹⁰² Yet, the IG acknowledges the agency still faces technological challenges, “Although the GAO removed the Modernization Program from its High Risk List, we believe the program remains a high risk and major management challenge for the IRS because of the needs for improvements in information technology practices and performance.”¹⁰³

Although USAspending.gov, in theory, should have paved the way for improved government transparency and technical know-how, the most recent struggle by the executive branch to implement the national health care exchange website may suggest otherwise. Further, while the Obama Administration has confidence in the Treasury Department to carry out the spending transparency website USAspending.gov, the Inspector General review notes IT weaknesses still exist at the agency. While it is unclear to what extent these internal IT failings would carry over to this proposal, these logistical concerns should be carefully considered in the context of asking the IRS to establish three new online databases.

Transparency Increase Freedom of Policymakers and the Public to Make Informed Decisions

¹⁰¹ “Annual Assessment of the Internal Revenue Service Information Technology Program (2012-20-126),” *Treasury Inspector General for Tax Administration*, September 30, 2013, 1.

¹⁰² “Annual Assessment of the Internal Revenue Service Information Technology Program (2012-20-126),” *Treasury Inspector General for Tax Administration*, September 30, 2013, 3-4.

¹⁰³ “Annual Assessment of the Internal Revenue Service Information Technology Program (2012-20-126),” *Treasury Inspector General for Tax Administration*, September 30, 2013, 21.

Increased access to the financial details of nonprofit organizations and any state and federal actions taken against questionable charities will begin to reverse the information asymmetry that exists in federal tax benefits directed to nonprofit entities. Correcting this failure will increase the freedom of lawmakers and laymen to make better decisions regarding the use of public and public funding directed to tax-exempt groups.

In an essay on the history of government transparency, the Sunlight Foundation highlights a long-held belief that with increased information comes increased freedom. “‘However firmly liberty may be established in any country, it cannot long subsist if the channels of information be stopped,’ Massachusetts Senator Elbridge Gerry stated in his fierce defense of providing federal subsidies to newspaper postal distribution in 1792.”¹⁰⁴

In its report on transparency and the tax-exempt sector, the Panel on the Nonprofit Sector acknowledged the “importance of transparency, of providing the information that allows the public to make informed choices and government officials to root out problems.”¹⁰⁵ The GAO echoes this sentiment, explaining, “Public availability of key information about the entities--i.e., transparency--can both enhance incentives for ethical and effective operations and support public oversight of tax-exempt entities, while helping to achieve and maintain public trust.” The government watchdog experts assert, “Thus, publicly available information helps establish a ‘free market’ in which charities compete for donations, which should encourage efficiency and effectiveness.”¹⁰⁶

Political Analysis

¹⁰⁴ Paul Blumenthal, “The History of Transparency – Part 1: Opening the Channels of Information to the People in the 1th Century,” *Sunlight Foundation*, March 23, 2010.

¹⁰⁵ “The Panel on the Nonprofit Sector, Strengthening Transparency Governance Accountability of Charitable Organizations,” *Independent Sector*, June 2005, 4.

¹⁰⁶ David M. Walker, “Governance, Transparency, and Oversight Are Critical for Maintaining Public Trust,” (Statement before the House Committee on Ways and Means,) *Government Accountability Office*, April 20, 2005, 12.

Every corner of the country is connected to the nonprofit sector. Whether it be professional sports, recreational associations and country clubs, or healthcare, banking, and education, nearly every American belongs to, participates in, or benefits from a tax-exempt entity. With this comes a wide array of political leanings in the nonprofit community, ranging from conservative religious groups to progressive service organizations. Given this reach, wading into an honest policy discussion about the nation's most beloved nonprofit organizations is a politically risky endeavor for any politician from either party. Through the auspices of transparency, however, this proposal provides a tenable first step in broaching the topic.

Congress

While the matter of nonprofit organizations is a politically sensitive topic, this proposal may creatively avoid some of the consternation associated with discussing radical changes to the tax treatment of certain entities or to the charitable deduction. The increased transparency requirements are designed to expose bad actors in the system and encourage taxpayers to hold these groups and the government accountable. Given this angle, the searchable databases and transparency provisions in this proposal may be more likely to enjoy general bipartisan support than other more punitive measures.

Transparency is generally a softer stick than more severe methods of punishment, such as simply terminating a program and slashing funding. Not only will this approach garner bipartisan backing simply based on policy, but it may also engender the political will needed from both sides that would be difficult to ascertain from more drastic action. While they may disagree on the substance of an issue, politicians from both parties will

typically coalesce around increased transparency and reporting requirements and efforts to modernize government.

For example, although two members may feel differently about government spending for education, they may find agreement in requiring the Education Department to disclose the full amount of federal assistance provided to each educational entity. This is demonstrated by broad bipartisan votes in favor of transparency measures similar to those included in this proposal. The Federal Funding Accountability and Transparency Act passed the Senate by unanimous consent, for example.¹⁰⁷

More recently, the April 2014 enactment of the Digital Accountability and Transparency Act (DATA Act) demonstrates that transparency legislation may be the most fertile ground for a legislative success in a time of extreme divisions in Washington. In a detailed expose on the process leading to the DATA Act's eventual passage, author Andrew Prokop acknowledges this bill was one of only a very few able to "make it through a gridlocked Congress."¹⁰⁸ The DATA Act, championed by Senators Mark Warner (D-Virginia) and Tom Coburn, and Republican Congressman Darrell Issa, made a number of changes to the USAspending.gov website and improved related government transparency requirements in current law. Despite months of tense negotiations, between these lawmakers, their staff, and the White House, eventually the DATA Act was signed into law.

Part of the DATA Act's success was due to the bipartisan nature of good government and transparency provisions, with republican and democrat advocates. The

¹⁰⁷ "S. 2590: Federal Funding Accountability and Transparency Act," Passed Senate with an amendment by Unanimous Consent, *United States Senate*, September 7, 2006.

¹⁰⁸ Andrew Prokop, "Beating the odds: Why one bill made it through a gridlocked Congress – and so many don't," *VOX*, May 22, 2014.

provisions of this nonprofit proposal should fall cleanly into a similar pattern, promoting transparency and open government, with the potential for support from members on both sides of the aisle.

The legislation would likely be referred to either the tax writing committees or the government reform committees, or possibly both. In any scenario there exists potentially fertile ground for the proposal in these committees in both the Senate and the House of Representatives, with the possible exception of the House Ways and Means Committee.

In the Senate Finance Committee, likely vocal supporters, who may even be inclined to introduce the legislation, include long time nonprofit watchdog and public disclosure advocate Charles Grassley, a republican from Iowa, as well as DATA Act cosponsor Mark Warner, democrat from Virginia. It is unlikely the ranking member, Republican Orin Hatch would be a significant roadblock, as only 11 states have few nonprofit entities in their borders than Utah. Meanwhile, California boasts the most nonprofit entities in the country, but no sitting members of the Finance Committee is from the Sunshine State.¹⁰⁹

Senate Finance Committee opposition is likely to come from Chuck Schumer (D-New York), as New York is home to the second most nonprofit entities.¹¹⁰ Maria Cantwell (D-Washington), will also likely strenuously oppose, as every person living in Washington state is eligible to be a member of the Boeing Employees' Credit Union, which with \$11.4 billion in assets, is now the fourth largest credit union in the United States.¹¹¹ Meanwhile, Democrat Bill Nelson is a wild card and could be crucial to the

¹⁰⁹ "Number of Registered Nonprofit Organizations by State, 2012," *National Center for Charitable Statistics*.

¹¹⁰ *Ibid.*

¹¹¹ "History and Mission - BECU.com" *Boeing Employees' Credit Union*.

proposals success or failure in the Senate Finance Committee. Florida ranks third in the listing of states with the most nonprofits.¹¹² However, the *Tampa Bay Times* investigation revealed extensive fraud throughout Florida charities, including the worst charity in America, which is located Holiday, Florida.¹¹³ With much state-level movement to address fraudulent charities, Ben Nelson's support could be key to committee passage in the Senate.

Finance Chairman Ron Wyden (D-Oregon), as well as the New Jersey and Texas members on any of the relevant committee, may raise objections, as their states are home to some of the largest and most profitable nonprofits, including the Kaiser Foundation in Oregon, New Jersey's Princeton University and the substantial university and health care systems in Texas. While their concerns may not be entirely alleviated, there are various options available to work toward compromise. One such variation would be to include other industries to be reviewed by the GAO-JCT study, instead of only including three.

The proposal's fate would be more uncertain in the House Ways and Means Committee. Committee Chairman Camp (R-Michigan) and Ranking Member Levin (D-Michigan) do not have any particular history with general transparency requirements for government actions and spending. Camp, however, included in his draft tax reform proposal, a number of changes to the tax treatment of nonprofit entities. These revisions are not necessarily related directly to the proposal under consideration, but did address to some extent, with the unrelated business income tax, the profitable nature of some tax-

¹¹² "Number of Registered Nonprofit Organizations by State, 2012," *National Center for Charitable Statistics*.

¹¹³ "America's Worst Charities - #1 Kids Wish Network," *Tampa Bay Times*, last updated July 17, 2014.

exempts.¹¹⁴ Generally, the committee is heavy with members from very pro-nonprofit states, including Texas, California, and New York-including the emphatic and persuasive Charlie Rangel.¹¹⁵ Another consideration is the possibility Congressman Paul Ryan (R-Wisconsin) will take the Ways and Means reins in the next Congress. While generally supportive of good government measures, his history with the Catholic Charities will certainly be a factor.

Both oversight committees, House Government Reform and the Senate Homeland Security and Government Affairs Committee, have a history of bipartisan cooperation, with a number of members committed to a transparent and efficient government. Both committees were intimately involved in passage of the DATA Act, and in previous government transparency efforts including the creation of USAspending.gov and Recovery.gov. Democrat Senators Tom Carper (Delaware) and Claire McCaskill (Missouri) both serve on the committee and have worked extensively in the past with Senator Coburn on legislation increasing government transparency and addressing fraud in various government programs. Meanwhile, Congressman Issa worked diligently on passage of the DATA Act and his team is well-versed in pushing transparency related legislation through their committee. With this broad history of support and previous work with outside sunshine advocacy groups, the government reform committees could play an integral role in pushing the proposal through to the White House.

Proposal advocates could focus on three specific issues in order to bring together a coalition of support from both sides of the aisle and mitigate any detractors as cautioned above. With the members from the right, proponents could emphasize the need for the

¹¹⁴ “Tax Reform Act of 2014: Discussion Draft: Section-by-Section Summary,” *House Committee on Ways and Means*.

¹¹⁵ “Committee Members, waysandmeans.house.gov,” *House Committee on Ways and Means*.”

proposal in the context of growing and expanding on open and honest government that is accountable to taxpayer and lawmakers alike. When navigating the concerns of those on the left, the proposal should appeal to the notion of “consumer protection” style improvements, designed to ensure those donating to charity are not conned by unscrupulous nonprofit executives or forprofit fundraises. With members of both parties, the proposal should be viewed as a measure to begin ensuring justice - that those hurting in our society have access to the charity being promised and that those who are skirting the law and stealing to add to their own wealth will be exposed.

While the proposal will likely have sufficient support in the relevant congressional committees, the prospect for floor consideration and eventual passage remains in question. As a bipartisan effort, it could be taken up and passed in both houses with relative ease most likely. However, as a smaller measure than most that receive independent floor time, if it could not garner unanimous support in the Senate, it would likely only be considered as part of a larger bill in the Senate. If a comprehensive tax reform bill were the only option for a vehicle, the proposal is unlikely to pass before the end of the 113th Congress.

The Obama Administration

Despite repeatedly purporting to be the “most transparent administration in history,”¹¹⁶ the Obama administration’s dedication to enacting new accountability measures or improving existing transparency requirements remains in question. While some government sunshine advocates are disappointed in the lack of progress made by the White House, and cite the difficulty of obtaining documents requested through the

¹¹⁶ Jonathan Easley, “Obama says his is ‘most transparent administration’ ever,” *The Hill*, February 14, 2013.

Freedom of Information Act as just one frustration. Yet, the administration puts significant effort into public relations initiatives designed to further the perception of an open government, the most notable of these is the “unprecedented release of more than 2 million White House visitor records.”¹¹⁷ Given this dichotomy, a proposal to require the IRS to post online information that is largely already publicly available, may be the necessary combination of workable transparency for this administration to lend at least cautious support.

The administration’s response to the DATA Act underscores the possible barrier that could exist to the proposal’s consideration by the executive branch. The DATA Act was a bipartisan effort in the Senate intended to modernize and improve USAspending.gov, which was the product of a joint effort from then-Senator Obama and Senator Coburn. During DATA Act negotiations, a leaked document with proposed changes to the legislation made by the Office of Management and Budget revealed the administration was largely opposed improving the clear shortcomings of the existing website. One analysis by the Data Transparency Coalition’s Hudson Hollister, went so far as to conclude,

These revisions reveal an effort by the White House OMB to undermine both the DATA Act and the President's own Open Data Policy. They also run contrary to the broad bipartisan consensus that has emerged across the political spectrum and in the House of Representatives for a comprehensive DATA Act that delivers real reform. ...But OMB's actions show it is opposed to the bill's central purpose of transforming federal spending into open data.¹¹⁸

The involvement of Democrat Senator Mark Warner was an essential component to DATA Act negotiations. While from the same party as the President, Warner was not

¹¹⁷ Josh Gerstein, “President Obama’s muddy transparency record,” March 5, 2012.

¹¹⁸ Hudson Hollister, “Leak Reveals White House OMB Effort to Remove Key Provisions from DATA Act,” *Data Transparency Coalition*, January 27, 2014.

afraid to publicly chide the administration when needed in order to nudge them to the negotiating table. He also understood the importance of moving the USAspending.gov website from the jurisdiction of OMB to the Treasury Department, who was more able to handle the work. For this proposal, which places the burden on the transparency burden largely on Treasury's IRS and will need support from this democrat White House, Warner's involvement could once again be needed. Advocates of the proposal will want to ensure Warner's support and active engagement, to help navigate any White House roadblocks.

Outside Advocacy Groups & Media

The transparency approach proffered in this proposal lends itself to a unique coalition of supporters from the left and the right. Left-leaning transparency groups as well as conservative government watchdog groups have long supported increased public access to the details of government activities and spending. A series of ongoing to transparency efforts, including those culminating with USAspending.gov and Recovery.gov, both which track government spending online, enjoyed widespread support during congressional consideration and administrative implementation.¹¹⁹

In 2006, a very active alliance of these types of organizations emerged to push lawmakers to enact the Funding Accountability and Transparency Act, which created the online database USAspending.gov. The legislation was supported "by leaders of both parties and an array of business, union, and watchdog organizations," and "was endorsed by over 150 organizations with a wide range of political leanings."¹²⁰ Based on details

¹¹⁹ Garrett L. Hatch, "The Federal Funding Accountability and Transparency Act: Implementation and Proposed Amendments," *Congressional Research Service*. February 3, 2009.

¹²⁰ Ibid.

provided by the office of Senator Tom Coburn, the Congressional Research Service described the coalition as follows,

The Senator's list of supporters included representatives of private enterprise, such as the U.S. Chamber of Commerce; unions, like the American Federation of State, County, and Municipal Employees; media groups, such as the American Society of Newspaper Editors; and government watchdog organizations, like OMB Watch. As evidence of the unusual alliance in support of S. 2590, the list indicated that both People for the Ethical Treatment of Animals (PETA) and Gun Owners of America supported the bill, as did both the National Gay and Lesbian Task Force and the Traditional Values Coalition.¹²¹

Similarly, just this year, a diverse group of 18 advocacy entities, including the left-of-center Citizens for Responsibility and Ethics in Washington and the right-leaning R Street Institute, formed a coalition to support the DATA Act transparency legislation, which became law earlier this year.¹²²

A coalition resembling these previous groups would likely emerge to support the proposal for increased access to government actions and financial details concerning nonprofit organizations. A few changes in the supporting groups would likely occur, however, based on the slightly different target for the increased transparency. While certain organization may not participate, new entities, such as tax reform advocacy groups, may join the effort. Further, while a few media outlets supported previous efforts, it is possible more news based groups may also join the coalition, given their general bent toward exposing public information.

As noted, some previous supporters of sunshine law may not endorse this proposal. Notably, nearly all of these organizations are in fact, nonprofit entities. As such, some may be more hesitant to support this level of internal sunshine, despite

¹²¹ Ibid.

¹²² Matthew Rumsey, "Diverse coalition unites to support strong DATA Act," *Sunlight Foundation*, February 11, 2014.

previously supporting government spending accountability efforts. This could be mitigated through one-on-one discussions with hesitant groups. These discussion should emphasize that increased sunlight on those groups with excessive revenue or assets, or fraudulent charities deceiving donors, will eventually redirect private donations and federal assistance to those groups with truly altruistic motives. In other words, supporting sunshine on the nonprofit sector may eventually benefit the groups with nothing to hide.

This proposal could gain a new variety of outside support from organizations advocating comprehensive tax reform. Though the transparency specific proposals are slightly tangential to tax reform, the findings from GAO's study on nonprofit hospitals, the credit union industry and educational institutions could pave the way for significant revenue on the table during tax reform. Groups like the Coalition for Comprehensive Tax Reform and the Committee for a Responsible Federal Budget, may lend support for this proposal as part of laying the groundwork for including nonprofits in the discussion of completely overhauling the tax code.

Conversely, a number of well-connected coalitions are actively lobbying Congress to preserve the charitable donation deduction and other tax benefits for nonprofit organizations, and others exist to defend the nonprofit status of many entities currently under scrutiny. Groups like the National Council of Nonprofits¹²³ and the Independent Sector are arduously tracking each tax reform proposal and the proposed changes to the nonprofit sector and could release an army of advocates to oppose any changes. It is possible, however, with member-level engagement, that these groups could be persuaded to support this proposal in lieu of actual changes to their tax-exempt status in the short run. Transparency could be viewed as the "third way" for these groups to find

¹²² "Key Provisions Affecting Nonprofits in the Camp Tax Reform Proposal," *Council on Nonprofits*.

common ground on a policy change that may be for them, less financially painful than a cap on the charitable deduction or an increase in the unrelated business income tax.

It is nearly certain most major nonprofit groups will oppose the proposal. However, a few creative and thoughtful charities who are willing to work with Congress instead of outright rejecting any proposal, may realize this transparency proposal could eventually send more private and federal financial assistance their direction. They could use it first as a way to avoid more drastic or immediate measures as part of tax reform. Even more, by enacting transparency provisions that will expose the wasteful and corrupt groups and hopefully result in revocation of their tax-exempt status, more private and public money would be funneled to the exemplary groups. Certainly those representing the three industries targeted in the GAO-JCT study would also oppose. It should be noted, however, that a simple GAO study is better than their nonprofit status being yanked by Congress without a full review.

American's Senator and the State of Oklahoma

For a serious senator and legislator who has been at the forefront of nearly every major policy battle during his ten years in the Senate, this proposal represents a departure from Senator Coburn's penchant to upend and completely overhaul every aspect of a known problem. Policy proposals drafted by Coburn's office range from a complete Social Security reform plan and a rewrite of existing Medicare and Medicaid laws, to the elimination of appropriation earmarks and numerous comprehensive deficit reduction proposals. With this drive to offer sweeping reforms and set a marker for a complete policy debate, it will be important to weigh one's personal feelings of leaving the Senate

after identifying significant challenges in the tax treatment of the nonprofit sector without offering a full scale solution.

The Coburn approach, however, has also long considered small first steps with broad bipartisan support, as the first chink in the armor for addressing these larger challenges. And often this method has proven a success. For example, the effort to eradicate earmarks began through transparency requirements. During his first year in the Senate, Senator Coburn forced a vote on an appropriations bill requiring all earmarks be listed in the committee report accompanying the bill. The first vote of this nature, held on September 21, 2005, passed by a vote of 55 to 39, with the support of 32 Republicans and 23 Democrats.¹²⁴ Only one day later, on the next appropriations bill, the same requirement passed by voice vote.¹²⁵ Six years later, House Republicans instituted a complete earmark ban.¹²⁶ The tax-exempt transparency proposal resembles this method of starting with a small, bipartisan area of agreement that will shine light on an existing issue and perhaps eventually move toward a more complete resolution.

For a retiring senator, there is little downside to offering a more complete solution, for Congress to consider in the wake of his departure. Some might ask why he did not call for more drastic measures, such as revoking the tax-exempt status of certain types of nonprofit entities or establishing new protocols requiring the IRS to more quickly address well-known areas of charity fraud. Yet, the short and long term effects of these actions are unknown at this time -particularly those associated with revoking the tax-exempt status of an entire sector of the economy. Senator Coburn often cautions

¹²⁴ “H.R. 2744: U.S. Senate Roll Call Votes 109th Congress – 1st Session: Question: On the Amendment (Coburn Amdt. No 1775),” *United States Senate*, September 21, 2005.

¹²⁵ “H.R. 2528: U.S. Senate Roll Call Votes 109th Congress – 1st Session: Question: On the Amendment (Coburn Amdt. No 1858),” *United States Senate*, September 22, 2005.

¹²⁶ Erin Kelly, “Some want earmarks back to help Congress pass bills,” *USA Today*, October 29, 2013.

against rushed congressional action to fix a problem without fully understanding both the challenge and the response. Were the proposal to address questionable tax-exempt organizations more punitive than the first step of commonsense transparency, some might later question the thoughtfulness of the author. This would run contrary to Senator Coburn's attention to detail in other policy areas and perhaps taint the view of his work in retrospect.

Recommendation

It is nearly impossible to read the news without learning of yet another scam artist hiding behind a fake charity in order to get rich off the generosity of unsuspecting donors. Just as frequent are the stories of wealthy executives of nonprofit organizations being paid millions of dollars, generating the ire of faithful patrons. Taxpayers, lawmakers, those who give of their personal means, and those in need of their help, each deserve a complete picture of the tax-exempt sector and this proposal begins that process. It is recommended Senator Coburn introduce the transparency legislation outlined in this proposal and work fervently to build broad bipartisan support for it before retiring from public office at the end of the year.

The proposal is simple, easily drafted, and would garner bipartisan support with little effort. It would require minimal staff and member-level time, but offers a potentially greater return than many policies. By introducing the legislation now and working to build internal support, the bill would likely be picked up by bipartisan watchdogs in the Senate and outside government transparency groups. Even if it does not pass before Senator Coburn's congressional exit, it is likely these advocates will reintroduce it in the

following Congress, as bipartisan opportunities are difficult to ascertain in the current environment.

Introducing the proposal before leaving the Senate also gives Coburn an opportunity to highlight a very serious area of tax law in need of reform. While some sitting members of Congress may be unwilling to broach the nonprofit community, a retiring senator has little to fear and may in fact be doing the tax writing committees in Congress a favor by calling attention to the egregious nature of some tax-exempt groups. There is a significant amount of federal revenue at stake with the tax-exempt sector, and should Congress reform the code, this potential revenue could be very valuable. It will be to their advantage that Senator Coburn has already mapped out the questionable behavior of many of these entities, and called for the use of public scrutiny to ensure only deserving groups retain a beneficial tax preference.

Similarly, while Congress continues to shirk its duty to reform the tax code, it would behoove them to gather information that would enable better decision making should the day of tax reform draw nigh. Given its unique combination of transparency, good government, and consumer protection, and in light of previous bipartisan efforts along these lines, this proposal has a higher probability than most of becoming law. If enacted, certain information would be made public and more easily accessible including the financial details of many tax-exempt entities, the state regulator actions taken against questionable charities, and the findings of a detailed government study on the impact of revoking the tax-exempt status of three prominent industries. These details would equip members of Congress in thoughtfully addressing this section of tax law, rather than lazily

capping the charitable deduction in order to generate revenue, while leaving in place inefficient and completely outdated tax-exempt laws.

Curriculum Vita

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